No. 1946

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

COLMAN COMPANY (a corporation),
Appellant,

vs.

T. W. WITHOFT, Trustee in Bankruptcy of the Estate of FRANK H. SWEENEY, Bankrupt,
Appellee.

In the Matter of
FRANK H. SWEENEY,
Bankrupt.

BRIEF FOR APPELLANT.

JOSEPH C. MEYERSTEIN,
Attorney for Appellant.

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Statement of Facts.

The voluntary petition of Frank H. Sweeney in this matter was filed on the 31st day of March, 1909, and the order of adjudication was made on the 1st day of April, 1909. The Colman Company and the bankrupt were liable together on a certain lease, the term of which at the date of the filing of the petition and of adjudication had not yet expired. On the

18th day of February, 1908, the Colman Company and the bankrupt entered into an agreement, the purpose of which was to impose upon each of the parties thereto a several liability as to one-half of the rental reserved in the lease. In other words, as between themselves, the Colman Company and the bankrupt agreed that each should be liable for one-half of the rent reserved, and no more. The agreement further recited: "And said parties hereto " agree and undertake, one with the other as surety " to the other against any liability or obligation for " any rent so reserved in said lease or the amount " thereof to which it may be reduced in excess of " one-half thereof."

Prior to the 1st day of February, 1909, and before the filing of the petition, the bankrupt and the Colman Company entered into a second agreement, by the terms of which it was provided that the Colman Company should enter into a contract with the lessors for the rescission of the lease, and the Colman Company was further empowered to pay for each and every month of the term provided in said lease remaining after the date of the rescission a sum not to exceed $100. The agreement further provided that the bankrupt should pay to the Colman Company one-half of the amount paid by the Colman Company, or agreed to be paid by it, as a consideration for the rescission of the lease. The Colman Company paid the rent for the month of April, amounting to $350, and shortly after the date of adjudication made an agreement with the lessors

whereby in consideration of the payment of $2400 the lease was canceled.

Under the terms of the agreement last referred to there thereupon became due from the bankrupt to the Colman Company one-half of this amount, or $1200. Adding to this sum one-half of the April rent paid by the Colman Company, we have a total of $1375; for which a claim was filed in proper form by the Colman Company. (Tr. pp. 4-17.) This claim was objected to by the Trustee in Bankruptcy, and after a full hearing and argument the objections were overruled, and the claim was allowed by the Referee in Bankruptcy. (Tr. p. 28.) The Trustee filed a petition for review of the order of the Referee allowing the claim, and the matter was thereupon heard on the certificate of the Referee and a stipulation as to the facts, by the District Court of the United States for the Northern District of California, and after hearing, the exceptions to the ruling of the Referee were sustained by the District Court and the claim disallowed. (Tr. p. 28.) From this order of the District Court made on the 5th day of December, 1910, appellant prosecutes this appeal.

Assignment of Errors.

1. The Court erred in sustaining the exceptions of T. W. Withoft, trustee of the estate of Frank H. Sweeney, bankrupt, to the order of the Referee al-

lowing the claim of said Colman Company, a corporation, in said proceeding.

2. The Court erred in not overruling the exceptions of said T. W. Withoft, trustee of the estate of Frank H. Sweeney, to the order of the Referee allowing said claim of said Colman Company, a corporation, as filed in said proceeding.

3. The Court erred in adjudging that the said claim of Colman Company, a corporation, as filed in said proceeding, was not a provable claim against the estate of Frank H. Sweeney, bankrupt.

4. The Court erred in not adjudging that the claim of Colman Company, a corporation, as filed in said proceeding, was a provable claim against the estate of Frank H. Sweeney, bankrupt.

5. The Court erred in disallowing and rejecting the claim of Colman Company, a corporation, as filed in said proceeding.

6. The Court erred in not adjudging that the claim of Colman Company, a corporation, as filed in said proceeding, was entitled to allowance under the provisions of Section 63, paragraph A, subdivision IV, of the Acts of Congress Relating to Bankruptcy.

Argument.

Practically, the question for determination here may be stated to be whether the claim of the Colman Company as filed is a provable claim under the pro-

visions of Section 63 of the Bankruptcy Act. The full text of that section is as follows:

> "Debts Which May be Proved. a. Debts of the bankrupt may be proved and allowed against his estate which are (1) a fixed liability, as evidenced by a judgment or an instrument in writing, absolutely owing at the time of the filing of the petition against him, whether then payable or not, with any interest thereon which would have been recoverable at that date or with a rebate of interest upon such as were not then payable and did not bear interest; (2) due as costs taxable against an involuntary bankrupt who was at the time of the filing of the petition against him plaintiff in a cause of action which would pass to the trustee and which the trustee declines to prosecute after notice; (3) founded upon a claim for taxable costs incurred in good faith by a creditor before the filing of the petition in an action to recover a provable debt; (4) founded upon an open account, or upon a contract, express or implied; and (5) founded upon provable debts reduced to judgments after the filing of the petition and before the consideration of the bankrupt's application for a discharge, less costs incurred and interest accrued after the filing of the petition and up to the time of the entry of such judgments.
>
> "(b) Unliquidated claims against the bankrupt may, pursuant to application to the court, be liquidated in such manner as it shall direct, and may thereafter be proved and allowed against his estate."

In the Court below the Trustee based his position on the line of cases holding that claims for future rents, or claims of a contingent nature, are not provable. Typical of this line of cases are Watson v.

Merrill, 14 A. B. R. 453, and the later case of Re Roth & Appel, 24 A. B. R. 588. These cases all go off on the proposition that a claim of the character of that under consideration in the cases just cited, is not a "fixed liability absolutely owing at the time " of the filing of the petition". An examination of the cases shows that they all ignore the fact that Subdivision 4 of Section 63a is co-ordinate with Subdivision 1 of the same section, and hence not controlled or limited by it. If this were otherwise, Subdivisions 2, 3 and 5 would be limited by Subdivision 1 as well as Subdivision 4. No such contention has ever been advanced, nor could it well be. For instance, Subdivision 2 provides for the proving of a claim

> "due as costs taxable against an involuntary bankrupt who was at the time of the filing of the petition against him plaintiff in a cause of action which would pass to the trustee and which the trustee declines to prosecute after notice".

How can the language of Subdivision 1 be read into Subdivision 2? In the very nature of things a claim arising under Subdivision 2 could not be a fixed liability absolutely owing at the time of the filing of the petition, for the reason that a claim under Subdivision 2 cannot arise until after the election of a trustee and until after a trustee has declined to prosecute an action passing to him after notice. Furthermore, there is no more reason for holding that the words "fixed liability absolutely " owing at the time of the filing of the petition"

should be interpolated in Subdivision 4 than that any other language in Subdivision 1 should be, as, for instance, "as evidenced by an instrument in writing". The absurdity of such a contention is apparent; yet it is just as logical as the reasoning which influences and governs the so-called rent cases.

There would be no difficulty in arriving at a decision in the case at bar if the same recognition were accorded to Subdivision 4 as is accorded to Subdivision 1, for it then becomes plain that *all* claims which are debts founded upon a contract, whether they be fixed liabilities at the time of the filing of the petition or not, are provable. The only limitation which with reason can be put upon the language of Subdivision 4 is that which would exclude a contingent claim where the contingency is of such a nature as to make it absolutely impossible to determine the amount at the time the proof is offered. This limitation, it must be noticed, would spring, not from the language of Subdivision 4 itself, but from the very nature of the claim.

This view finds abundant support n the Bankruptcy Reports. One of the leading cases dealing with this class of claims is

Moch v. Market St. Nat. Bank, 6 A. B. R. 11 (Ct. Ct. App., 3rd Ct.),

holding that where the liability of an endorser of commercial paper does not become fixed and absolute until after his bankruptcy, it may still be proved against his estate if such liability has become fixed

within the time limited for proving claims. It is interesting to observe that the Court in the course of its opinion uses the following language:

> "The first and fourth subdivisions of Section 63 are *distinct* provisions, and are, we think, *independent* of each other. We are unable to agree with the proposition that subdivision 1 qualifies, and is to be carried down and read into subdivision 4. *On the face of the act they are distinct.*" (Italics ours.)

In Cobb v. Overman, 6 A. B. R. 324 (Ct. Ct. of App., 4th Circuit), the Court held that a bond given to secure the payment of an annuity in force at the date of the filing of the petition against the obligor, is a provable debt against his estate. The ruling in favor of provability in this case was made although it was necessary to calculate the expectancy of the annuitant in order to fix the liability. Furthermore, the Court did not look to Subdivision 4 to find its reason for the decision, but based its holding on the narrow language of Subdivision 1.

> (See, in this connection, Hibbard v. Bailey, 12 A. B. R. 104.)

Along the same lines is the language found in In re Swift, 7 A. B. R. 374-381 (Ct. Ct. of App., 1st Ct.):

> "Under some bankruptcy statutes provision was made for liquidating the present values of contingent debts and contingent liabilities for provable purposes, but the present statute does not expressly provide any machinery for that purpose. *It provides without apparent restriction for proof of debts founded on contracts express or implied.*" (Italics ours.)

The case of In re Smith, 17 A. B. R. 112, is a case thoroughly and carefully reasoned, and unless the language of the opinion there can be successfully challenged or controverted (which we doubt) we deem the case to be conclusive of the question involved here. The Smith case, like the Moch case, was one arising out of an endorsement of notes which did not mature until after the date of adjudication, although at the date of proof the notes had matured. It was said by the Judge:

> "The claims in question are clearly within the terms of subdivision 4. This was the view of the learned judge in Re Gerson (D. C.), 5 Am. B. R. 89, 105 Fed. 891, affirmed by the Circuit Court of Appeals for the Third Circuit in Moch v. Market Street National Bank, 6 Am. B. R. 11, 107 Fed. 897. The latter case was cited in the opinion of the Supreme Court in Dunbar v. Dunbar, 190 U. S. 340, 350, 351, 10 Am. B. R. 139, 47 L. Ed. 1084. While Moch v. Market Street National Bank was neither approved nor disapproved, the opinion of the Supreme Court points out the precise point decided—i. e., that under section 63a, subd. 4, the creditor might prove against the estate of the bankrupt after the liability had become fixed. Moreover, it may be fair to say that the course of reasoning, wherein distinctions are made between classes of contingent claims, would hardly have been necessary had the Supreme Court been of the opinion that, upon a proper construction of section 63, all claims which had been contingent at the time of filing the petition were excluded from allowance, though no longer contingent at the date of proof. See, also, In re Rothenberg (D. C.), 15 Am. B. R. 485, 140 Fed. 798; Collier on Bankruptcy (5th Ed.), pp. 484, 489.

"But, aside from authority, and upon an independent reading of section 63, I am of the opinion that neither grammatical nor logical reasons require that subdivision 4 shall be limited by subdivision 1. It is very clear that subdivisions 1, 2, 3, 4 and 5 are not to be regarded as an enumeration of a group of characteristics, all of which are essential to a provable claim. On the contrary, the subdivisions specify separate classes of provable claims. It is a classification." (Italics ours.)

"It is argued that, because subdivision 1 specifies a fixed liability absolutely owing, it excludes all liabilities which were contingent at the time of filing the petition from proof under other subdivisions. The logical fault is obvious. While contingent liabilities are excluded from class 1(defined by subdivision 1), it does not at all follow that liabilities now or formerly contingent are excluded from other distinct classes. The specification of certain characteristics for class 1, is no indication that cases comprehended in other classes may not have entirely different characteristics. Assuming that, so long as it is uncertain whether a contract or engagement will ever give rise to an actual liability, and that so long as the demand is contingent, it is not provable, it by no means follows that a demand which has ceased to be contingent before proof should be rejected because it had been contingent before the date of filing the petition. While the language, 'Debts of the bankrupt * * * which are * * * founded upon an open account, or upon a contract express or implied', may not include contingent obligations, it does include obligations no longer contingent, though they were contingent at the date of filing the petition.

"It has been argued that the only reasonable construction which can be given to subdivision 4 of section 63 is that it refers to claims upon

> which a right of action has accrued at the time of the filing of the petition, and that to construe it as permitting proof of contingent claims is to make subdivision 1 superfluous and useless. It is to be observed, however, that the claims here in question, when proved, were no longer contingent; they had become present liabilities through the fact of non-payment and protest. There is no necessary inconsistency between a class which includes and provides for liabilities absolutely owing at the time of filing the petition, whether then payable or not, and a class of liabilities which includes debts which mature after the time of filing the petition. It does not follow, because contingent liabilities are excluded from the first group of classification, that liabilities founded upon express contracts, and which are no longer contingent at the date of proof of such liabilities, are not included within subdivision 4. It does not involve logical inconsistency to hold that subdivision 4 comprehends claims which are expressly excluded from subdivision 1, or even to hold that subdivision 4 includes claims contained within subdivision 1, as well as many others. A series of broadening classes is not unusual, and inclusion of a smaller class in a broader class is not inconsistency."

The excerpts from the Smith case have been thus freely borrowed because they constitute in themselves a convincing and, we believe, an unanswerable argument in support of the claim before the Court here. In our case, like in the endorser cases and surety cases, the liability became fixed within the time limited for the proof of claims. It certainly was as much a fixed liability at the date of the filing of the petition as that of an endorser on a promissory note or the surety on a bond. A surety might

never be called upon to pay; neither might an endorser. The liability of an endorser might be less than the face of the note; the liability of a surety might be less than the penalty expressed in the bond. Of course the liability of an endorser could not be more than the face of the note with interest, nor that of a surety more than the penalty expressed in the bond. So in our case the claimant might have paid to the lessors a sum less than that specified in the agreement with the bankrupt; he could not pay more and charge the bankrupt.

If the claims against endorsers and sureties are held to be provable where the liability becomes fixed after the filing of the petition, how can provability be denied to the claim here, where, as in the cases cited, the liability became fixed by the happening of the contingency, within the time limited for the proof of claims? It certainly is just as much a claim founded upon contract; and though the same element of doubt as to its ultimate amount existed at the date of the filing of the petition, it became fixed absolutely within the time limited for proof.

We feel perfectly safe, therefore, in resting upon the decisions to which attention has been called, and most of which, it will be noticed, are the views of Circuit Courts of Appeal. To the cases already cited may be added

In re Semmer Glass Co., 14 A. B. R. 25 (Ct. Ct. of App., 2nd Ct.);

In re James Dunlap Carpet Co., 20 A. B. R. 882.

As stated at the outset, there is a line of cases which holds that the limitations of 63a, Subdivision 1, should be carried down into the other subdivisions of the section. It will serve no purpose to review these cases, because, as said by the learned judge of the lower Court in an informal oral opinion (not made part of the record because not filed), "Upon " this question the authorities are in hopeless con- " flict, and nothing but a decision of the Court of " Appeals of this circuit will settle the law". So, also, said Judge McPherson, who in the case of

Re Caloris Mnfg. Co., 24 A. B. R. 611,

used the following language:

> "The claimant filed its proof of debt on Feb. 23, 1910, for $6,166.67, this being the difference between the amount of rent for the two terms. The referee disallowed the claim on the authority of Re Roth and Appel (D. C., N. Y.), 22 Am. B. R. 504, 174 Fed. 64, and the decision undoubtedly sustained his position. I cordially agree with Judge Hough that the conflicting decisions on this subject are in a state of 'hopeless confusion', and that an authoritative decision is much to be desired. Certainly, neither he nor I can give it, and it will probably need the intervention of the Supreme Court before the inferior tribunals will know what rule to obey. Meanwhile, however, I think the principle of Moch v. Market Street Bank (C. C. A., 3rd Cir.), 6 Am. B. R. 11, 107 Fed. 897, governs the district courts of this circuit, and requires us to hold that even although the landlord's claim in the present case was not a fixed liability under section 63a (1) when the petition was filed it was liquidated within the year and thus became provable as a claim founded upon a con-

> tract express or implied under section 63a (4). The case of Moch was followed in Re Dunlap Carpet Co. (D. C., Pa.), 20 Am. B. R. 882, 163 Fed. 541, and I shall adhere to that ruling until its error is definitely established."

There is not a word in any of the cases relied upon by appellant which limits the decisions to cases of commercial paper. This is referred to now because some effort at such a contention was made by appellee below. Nor is there any difference in principle between the liability of an endorser and the liability of the bankrupt here to claimant. The effort of some Courts to draw such a distinction illustrates a certain looseness of reasoning in the case most relied on by appellee. (Re Roth & Appel, supra.) In the course of his opinion Judge Noyes says:

> "It is not necessary for the purposes of the present case that we should go so far as to dispute the conclusions reached in these decisions. While a contract of indorsement is contingent, the extent of the liability is at all times ascertainable, and it might be that such a contract would be provable without it following that an indemnity contract covering possible loss of rents—both the existence and extent of liability upon which are uncertain and contingent—would be provable."

It requires no argument to controvert the statement that, "While a contract of indorsement is con- " tingent, the extent of the liability is at all times " ascertainable". An endorser may never be called upon to pay, or may be never legally compellable to

pay, or may be called on only in part. All this is true of the liability of the bankrupt here.

The same looseness appears throughout these decisions in their references to the language of the section, when, under the circumstances, it should be most carefully scrutinized. Cardinal rules of interpretation require that the utmost precision be used in giving effect to the entire phrasing of the statute. Yet we find important words omitted. Subdivision 1 does not require that the debt should be "a fixed "liability absolutely owing at the time of the filing "of the petition", but "a fixed liability absolutely "owing at the time of the filing of the petition "*against him*" (the bankrupt). It is true that Section I, subdivision 1, provides that, "'A person "against whom a petition has been filed' shall in-"clude a person who has filed a voluntary petition". But by no stretch of judicial reasoning could this warrant the conclusion that the time of filing a voluntary petition is the same as the time of filing an involuntary one. Undeniably subdivisions 1 and 2 of Section 63a refer to involuntary cases only and have no application to the case at bar. Regarding this distinction, important as it is, the cases are all silent.

It necessarily follows that the only restriction on subdivision 4 of section 63a is that the claim be *a debt*. That the claim here in question is a debt will hardly be questioned. Appellee, himself, in a brief filed below, draws his definition of the term "debt"

from Loveland on Bankruptcy, 3rd Edition, page 339. We adopt it cheerfully. It follows:

> "The word 'debt' seems to have been used in other bankruptcy acts, as defined by Mr. Justice Blackstone. He said: 'The legal acceptation of debt is a sum of money due by certain and express agreement, as by a bond for a determinate sum; a bill or note; a special bargain; or *rent reserved on a lease;* where the quantity is fixed and specific and does not depend upon any subsequent valuation to settle it.' That this is the sense in which 'debt' is used in this section is fairly to be inferred from the context."

According to this definition, "rent reserved on a lease" is a debt. Consequently an agreement to pay half of it and later to compound it at not to exceed a given sum, would be equally so.

In view of the fact that in the Court below it was suggested by counsel for the Trustee that claimant here had no authority, after adjudication, to make a settlement with the lessors, it may be well before closing to say a few words upon this point. In the first place, even leaving out of consideration the irrevocable delegation of authority which the contract contained, the contract as such could not be terminated by a mere adjudication of bankruptcy. This much is held in unequivocal terms in the case of Watson v. Merrill, supra, dealing with the question of future rents. When, however, there is taken into consideration the fact that the Colman Company itself had an interest in the lease—in other words, in the subject matter concerning which it was to exercise a

power conferred by the bankrupt, it is clear that the authority was not, and could not be revoked by bankruptcy, or even death. It is a general rule that where a power of attorney is given for a valuable consideration, or is coupled with an interest, or is part of the security for the payment of money or performance of some other lawful act, it is irrevocable whether so expressed on its face or not.

Frink v. Roe, 70 Cal. 296;
Norton v. Whitehead, 84 Cal. 262.

For the reasons stated, therefore, we submit that the claim should have been allowed as filed, and that the order of the District Court sustaining the Trustee's exceptions to the order of the Referee, should be reversed.

Respectfully submitted,

JOSEPH C. MEYERSTEIN,
Attorney for Appellant.